

The sale of an integrated computer and printer system for the printing of digital images is graphic arts machinery and equipment exempt from Retailer's Occupation Tax and Use Tax. See 86 Ill. Adm. 130.325. (This is a PLR.)

June 14, 2006

Dear Xxxxx:

This letter is in response to your letter dated December 8, 2004 as supplemented by your letter of January 3, 2006. The Department issues two types of letter rulings. Private Letter Rulings ("PLRs") are issued by the Department in response to specific taxpayer inquiries concerning the application of a tax statute or rule to a particular fact situation. A PLR is binding on the Department, but only as to the taxpayer who is the subject of the request for ruling and only to the extent the facts recited in the PLR are correct and complete. Persons seeking PLRs must comply with the procedures for PLRs found in the Department's regulations at 2 Ill. Adm. Code 1200.110. The purpose of a General Information Letter ("GIL") is to direct taxpayers to Department regulations or other sources of information regarding the topic about which they have inquired. A GIL is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120. You may access our website at [www.tax.illinois.gov](http://www.tax.illinois.gov) to review regulations, letter rulings and other types of information relevant to your inquiry.

Review of your request disclosed that all the information described in paragraphs 1 through 8 of Section 1200.110 appears to be contained in your request. This Private Letter Ruling will bind the Department only with respect to COMPANY for the issue or issues presented in this ruling, and is subject to the provisions of subsection (e) of Section 1200.110 governing expiration of Private Letter Rulings. Issuance of this ruling is conditioned upon the understanding that neither COMPANY nor a related taxpayer is currently under audit or involved in litigation concerning the issues that are the subject of this ruling request. In your letter you have stated and made inquiry as follows:

ABC has asked us to assist them in obtaining a private letter ruling for COMPANY. In connection therewith, I am enclosing ABC's request for ruling together with a Power of Attorney authorizing INDIVIDUALS of ABC and myself to represent COMPANY before the Department in connection with the enclosed request for ruling.

Please give me a call before the end of the year to let me know when we might expect you to address our ruling request. Of course, should you have any questions, please do not hesitate to call.

The letter from ABC reads as follows:

We represent COMPANY in connection with this Request for Administrative Ruling.

**Issue**

Whether sales of COMPANY's Picture Maker Thermal Print Station are exempt from Retailers' Occupational Tax liability under Illinois law.

### **Facts**

COMPANY founded and built its nation-wide business on the manufacture of conventional film and the processing of that film using silver haloid wet processes. Recent developments in the industry, however, are changing the very nature of film and the methods in which photographs are produced. Digitized images are taking the place of traditional film, and conventional film processing is swiftly being replaced by thermal printing. In response to these developments, COMPANY is presently introducing new technology in the form of a machine that manufactures photographic prints through procedures vastly different from traditional film processing.

**Picture Maker Thermal Print Station:** The Picture Maker Thermal Print Station ("TPS") operates as a machine offering several options for printing photographs. The TPS does not develop photographic images through traditional film processing methods. Instead, the images are digitally uploaded and then printed using thermal technology. The TPS utilizes digital and thermal capabilities to print media transmitted from a variety of sources, including picture cds, digital memory cards, camera phones, and even the Internet. The TPS's additional features include an attachable unit enabling the capabilities of the TPS to be available for 35mm film and one-time use cameras. In all cases, the media is transmitted into the TPS, whether it is physically inserted (as in the case of a digital memory card or a picture cd), e-mailed (as in the case of an Internet signal) or sent from a camera phone. The media is digitally uploaded to the TPS internal computer, and the stored images are then transferred to special paper for printing. This transfer is achieved through thermal processes. Digital input activates a thermal system that immediately heats color ribbon to such a degree that the ribbon is melded with the special print paper, thereby transferring the digitized image. The color ribbon is consumed in the process, and a photographic print is the result. In addition to the prints, the customer receives an index print and a picture cd containing a file of each image. Traditional negatives are not produced.

The TPS's thermal printing capabilities enable multiple digital photographs to be printed in less than 10 minutes. These same capabilities allow for the manufacture of other outputs such as identity badges and greeting cards. The process is similar to offset printing in that digital algorithms serve as the intermediary between the exposed image and the thermal output.

TPS machines are typically purchased or leased by retail stores, which place them within their internal photography centers. The machine is maintained through frequent exchange of photographic paper, cds, thermal cartridges and paper chads, and frequent removal of recyclable materials such as discarded film cartridges from the TPS's main accessory. Involvement by retail store personnel is required for all maintenance. Retail store personnel also provide supervision over the operation and security of the TPS machines by performing a variety of duties, including programming a password option that is offered as an extra TPS feature, and by monitoring for copyright infringement. Employees also maintain separate billing records for all receipts generated by TPS activities.

### **Applicable Law**

Illinois imposes a sales tax, designated the Retailers' Occupational Tax, on retail sales of tangible personal property. 35 Ill. Comp. Stat. 120/2 (2004).

\* \* \*

Illinois particularly exempts from Retailers' Occupational Tax liability graphic arts machinery and equipment certified by the purchaser to be used primarily for graphic arts production. 35 Ill. Comp. Stat. 120/2-5(4) (2004). Graphic arts production includes digital printing. Ill. Adm. Code tit. 86, § 130.325(b)(1)(D) (2004). Digital printing includes printing of what is commonly known as digital photography. The process is described as use of a qualifying integrated computer and printer system to print a digital image. *Id.* at (b)(1)(E). Graphic arts production also includes preliminary processes that manipulate images in preparation for printing. Such processes include color separation and image assembly. *Id.* at (b)(4)(A).

Illinois does not limit the graphic arts exemption to organizations involved in graphic arts production. Illinois Administrative Code §130.325(b)(1)(C)(2004) states that "The [graphic arts] exemption is not limited to qualifying equipment used by the establishments described in the NAICS [North American Industry Classification System], but rather to qualifying machinery and equipment used in the printing processes described in the NAICS (for example, lithography, gravure, flexography, screen printing, quick printing, digital printing and trade services such as prepress and binding and finishing services)."

### **Analysis**

Sales of the TPS should be exempt from Retailers' Occupational Tax liability because the purpose and design of the TPS clearly fits within the graphic arts exemption allowed by Illinois law.

The TPS produces tangible personal property by printing digitally transmitted images. It houses a complete and integrated production system that is able to change the form of tangible personal property (digital media or 35mm film) into something entirely different from that in which it was acquired (photographic prints). The TPS initiates and sustains the entire transformation, from the point of insertion of raw material to the printing of the photographs to be sold at retail. Whether the exposed image initially rests in a 35mm camera, digital camera, picture cd, or Internet attachment, the design of the TPS and the function of its added features enables the same digitized process to occur. The finished product does not simply appear altered; its composition is entirely different. The single purpose of the TPS is to initiate and sustain this entire transformation.

The functions of the TPS allow it to squarely fit within the graphic arts exemption allowed under Illinois law, because as a result, digital photography is printed. Transformation of the media and printing of the photographs entirely depend upon these internal functions. But for them occurring, photographs would not be printed. The operation cannot be aligned with traditional film processing because chemical by-product does not result, and traditional film negatives are not created. Nor can the process be aligned with xerographic copying, because the raw material and the end product are entirely different in composition and character. A copy is not being created, but instead an entirely new saleable good is being produced that in no way resembles

the raw material from which it derived. The process is transparent and highly integrated in terms of purpose, functionality, and timing.

The Illinois Department of Revenue issued a General Information Letter No. ST 99-0333-GIL in November of 1999, which stated that an Image Magic Picture Maker ("Picture Maker") would qualify for exempt status under the graphic arts exemption. The TPS is very similar to the Picture Maker, but it also offers increased production capabilities and features including the ability to accept input from camera phones and the Internet. However, both machines produce tangible personal property through the use of digital means to accept input and thermal means to manufacture output. In addition, the General Information Letter was written on the understanding that the Picture Maker was operational within a retail environment. The tax-exempt recommendation did not appear to hinge on the business of the Picture Maker's owner. The inherent similarities of the Picture Maker and the TPS in functionality and placement lend strong support to our belief that the Department of Revenue's opinion on the exempt status of the Picture Maker should also extend to sales of the TPS.

For the above-stated reasons, we believe sales of the TPS should be exempt from Illinois Retailers' Occupational Tax liability.

### **Disclosures**

1. The tax period at issue in this request begins at the 2004 fiscal year and extends to the present time. COMPANY is not presently under audit with the Department of Revenue.
2. To the best of COMPANY's and ABC's knowledge, the Department of Revenue has not issued a ruling on the taxability of Thermal Print Stations or other similar machines for COMPANY. In addition, neither COMPANY nor any representative of COMPANY previously submitted the same or similar request to the Department and subsequently withdrew the request before a letter ruling was issued.
3. COMPANY and ABC have determined, to the best of their knowledge, that there are no authorities in Illinois law that are contrary to the views expressed in this request for an administrative ruling.
4. The facts in this request for an administrative ruling do not constitute trade secret information, and therefore, do not need to be deleted from the publicly disseminated version of the private letter ruling.

### **Conclusion**

With respect to the foregoing discussion, we respectfully request the following administrative ruling:

1. Sales of the TPS and its added features are exempt from Illinois Retailers' Occupational Tax liability.

If the Department of Revenue reaches a tentatively adverse opinion we request a conference on the matter. If the Department of Revenue ultimately concludes that its opinion will be adverse, COMPANY reserves the right to withdraw this Petition prior to the issuance of the adverse opinion.

If you have any questions on this matter, please contact PERSON ABC.

Thank you for your assistance on this matter.

In your supplemental letter of January 3, 2006, you have stated as follows:

In connection with the above captioned private letter ruling request, you recently raised some additional questions. Below are our responses to your questions. I have restated the questions for your convenience.

1. How does the G3/TPS attachment enabling TPS capabilities to be available for 35mm film and one-time use cameras work? Does the process differ from traditional photoprocessing? In other words, does the process differ from the production of prints transmitted via other media (digital memory card, internet signal, camera phone etc.)?

ANSWER: The 35 mm film and one-time use camera attachment is called the Film Processing Station ("FPS"). The FPS process is a modification of the traditional film process. In the FPS process, a thin layer of developer is applied to the film and the film is scanned during the development process. After scanning, the film is destroyed and no negative is produced. (In a normal film process, developer and other solutions are applied to the film that develop a color negative dye image on the film. The film is then dried and the resulting negative can be subsequently be [sic] scanned or printed optically.) The FPS process is faster, and uses much less chemistry than conventional processing.

After a film image has been scanned, the process the kiosk uses for printing the image is very similar to that used for other digital inputs, such as camera cards or CDs.

2. Can the attachment for the 35mm film be purchased separately from the body of the G3/TPS? In other words, is it marketed as an option?

ANSWER: COMPANY had intended to market the FPS attachment as a separate optional accessory to the thermal printing kiosk. Unfortunately, trade trials did not yield a good return. As a result, the FPS product was never sold.

I trust that these responses to your questions will enable you to complete your work on COMPANY's private letter ruling request. If there is anything else you need, please let me know.

## **DEPARTMENT'S RESPONSE:**

The Department's regulations for the Graphic Arts Machinery and Equipment Exemption can be found at 86 Ill. Adm. Code 130.325. The Graphic Arts Machinery and Equipment Exemption extends to machinery and equipment that is used primarily in graphic arts production. "Graphic arts production" is defined in this regulation as "printing, including ink jet printing, by one or more of the processes described in Groups 323110 through 323122 of Subsector 323, Groups 511110 through 511199 of Subsector 511, and Group 512230 of Subsector 512 of the North American Industry Classification System published by the U.S. Office of Management and Budget, 1997 edition." (86 Ill. Adm. Code 130.325(b)(1)(A)) The Section goes on to state that "[g]raphic arts production does not include (i) the transfer of images onto paper or other tangible personal property by means of photocopying or (ii) final printed products in electronic or audio form, including the production of

software or audio-books.” These provisions come directly from the statutory language found in the Retailers’ Occupation Tax Act at 35 ILCS 120/2-5(4) (exemption for graphic arts) and 35 ILCS 120/2-30 (definition of “graphic arts production”) and the Use Tax Act at 35 ILCS 105/3-5(6) (exemption for graphic arts) and 35 ILCS 105/3-10 (definition of “graphic arts production”).

Groups 323114 and 323115 of Subsector 323 the North American Industry Classification System, which are specifically included in the exemption, are, respectively, “quick printing” and “digital printing”. The Department’s rule at 130.325(b)(1)(E) states that “[d]igital printing and quick printing” mean the printing of graphical text or images by a process utilizing digital technology . . . . It also includes the printing of what is commonly known as “digital photography” (e.g., use of a qualifying integrated computer and printer system to print a digital image).” COMPANY’s Picture Maker Thermal Print Station and its added features is an integrated computer and printer system for the printing of digital images. When used as described in this ruling request the Picture Maker Thermal Print Station and its added features is used primarily in graphic arts production and, when sold for such use, qualifies for the graphic arts exemption.

The factual representations upon which this ruling is based are subject to review by the Department during the course of any audit, investigation, or hearing and this ruling shall bind the Department only if the factual representations recited in this ruling are correct and complete. This Private Letter Ruling is revoked and will cease to bind the Department 10 years after the date of this letter under the provisions of 2 Ill. Adm. Code 1200.110(e) or earlier if there is a pertinent change in statutory law, case law, rules, or the factual representations recited in this ruling.

I hope this information is helpful. If you have further questions concerning this Private Letter ruling, you may contact me at (217) 782-2844. If you have further questions related to the Illinois sales tax laws, please visit our website at [www.tax.illinois.gov](http://www.tax.illinois.gov) or contact the Department’s Taxpayer Information Division at (217) 782-3336.

Sincerely,

Samuel J. Moore  
Associate Counsel

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